

A11-2093

**State of Minnesota
In Supreme Court**

County of Ramsey,

Relator,

v.

Federated Retail Holdings, Inc.,

Respondent.

**REPLY BRIEF OF
RELATOR COUNTY OF RAMSEY**

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TABLE OF CONTENTS

INTRODUCTION..... 1

REPLY TO RESPONDENT’S ARGUMENT..... 4

I.The tax court did not have, and did not need, jurisdiction over Parcel 0005 4

**II.The rights to the use of the Leased Basement Space run with the land of the
Subject Property, Parcel 0004..... 5**

**A. The Subject Property’s right to use the Leased Basement Space is
assignable without the need to execute additional instruments..... 5**

1. The terms of the Lease..... 6

2. Conduct of the parties..... 6

**B. The holding of County of Du Page supports Relator’s argument that
property values for tax purposes should reflect the benefits provided
by an adjoining parcel. 7**

**C. Leased fee and leasehold estate have no applicability to the valuation
of Parcel 0004..... 9**

III.Taxation of Parcel 0005 is not at issue..... 10

CONCLUSION..... 10

CERTIFICATE OF COMPLIANCE..... 12

TABLE OF AUTHORITIES

CASES

Continental Retail v. County of Hennepin, 801 N.W.2d 395 (Minn. 2011)..... 9

County of Du Page v. Property Tax Appeal Board, 660 N.E.2d 985 (Ill. App. Ct.
1995)..... 7, 8, 9

County of Du Page v. Property Tax Appeal Board, 708 N.E.2d 525 (Ill. App. Ct.
1999)..... 7, 8, 9

Homer v. Dadeland Shopping Center, Inc., 229 So.2d 834 (Fla. 1969) 8

STATUTES

Minnesota Statutes § 272.03 10,11

Minnesota Statutes § 272.16 4

INTRODUCTION

Before responding to Respondent's arguments, Relator is compelled to address Respondent's Statement of Facts. Respondent implies that it pays substantial amounts as rent for the Leased Basement Space. Resp. Br. at 6. Respondent's statements are misleading. Respondent quotes from Article 10 of the Lease, but fails to point out that the last paragraph of Article 10, Paragraph E states:

Notwithstanding the provisions of this Article, Tenant's obligations as to taxes shall be as provided in the Supplemental Agreement, as amended, between the parties hereto ("Supplemental Agreement") as long as the Premises are taxed with the Main Store. If the Premises are at any time not taxed with the Main Store, the terms of Subsections A-D of this Article 10 shall be applicable.

Rel. App. at 16.

An unsigned draft of the Lease shows that everything up to paragraph E is the standard lease language that the mall used, presumably for leases with its in-line stores. *See* Ex. K, Tab 3 at P-000268 to P-000269. But, this is not an in-line tenant, and this is not an ordinary lease. When this Lease was entered, paragraph E was added to Article 10 to be consistent with the intention of the parties to have the value of the Leased Basement Space "taxed with the Main Store." *See* Ex. K, Tab 3 at P-000268 to P-000269; Rel. App. 16.

Having the Leased Basement Space taxed with the Main Store is also consistent with the language in Article 12 that states that "it is understood and agreed that the square footage of the Premises shall be included as Gross Floor Area of the Main Store for the

purposes thereof,” referring to the Rosedale ROOA. Rel. App. at 16. That same Gross Floor Area of the Main Store, which includes the Leased Basement Space, is the determinative area for purposes of the Shopping Center Merchants Association as described in Article 14. Rel. App. at 17.

The language of these provisions of the Lease likewise is consistent with the assessor’s records which show a transfer of the value of a portion of the former store on Parcel 0005 to Parcel 0004 (the Subject Property) in 1992. Rel. Add. at 65–66. The statements of Mr. Dahlen indicate that this allocation of value is how the value has been taxed since then. Tr. at 380–81. These exhibits and testimony support the fact that the value of the Leased Basement Space was being taxed as part of the value of the Subject Property pursuant to Paragraph E of Article 10 of the Lease, not as a tax on the basement space paid to the mall owner pursuant to Paragraphs A through D of Article 10. Because “the Premises” were being “taxed with the Main Store” for the assessment dates at issue, Paragraph E of Article 10 controlled. The language Respondent quotes from Paragraph A of Article 10 was not applicable.

The footnote on page 6 of Respondent’s Brief is likewise inaccurate in that there is no evidence that any “taxes” were ever paid to the Landlord under Article 10 of the Lease. Rather, real estate taxes were paid to the county by Respondent on the Leased Basement Space because its value was included in the Subject Property for property tax purposes.

Furthermore, any “common area costs and expenses” paid to the mall owner are pursuant to the Restatement of Operating Agreement (“ROA”) between Respondent and the mall owner, not pursuant to Article 12 of the Lease which states “All rights and obligations of the parties as to the Common Area shall be as set forth in the Rosedale ROOA, it being understood and agreed that the square footage of the Premises shall be included as Gross Floor Area of the Main Store for the purposes thereof.” Rel. App. at 16. “Such costs and expenses shall not include real estate taxes or special assessments.” Resp. Add. at 6. Payments under the ROA relate to expenses of the common area, not expenses of the Leased Basement Space. They are contributions required of all department stores at the mall by the ROA. Resp. Br. at p. 6; Resp. Add. at 3–7. These payments relate to the Macy’s store’s share of the expenses of the mall common area and as such cannot be characterized as “rent” for the Leased Basement Space. It is misleading to characterize any of the amounts stated on page 6 of Respondent’s Brief as “rent” paid to the Landlord for the Leased Basement Space.

Finally, Respondent leaps from the fact that the Lease is assignable to the unsupported conclusion that the “Leased Basement Space may be used by a different user than the user of Parcel 0004.” Resp. Br. at 6, 14. That conclusion is directly contradicted by the terms of the Lease that require the following: “(3) PERMITTED USE: Premises shall be used by the Tenant solely for an integrated part of the operation of Tenant’s department store operated adjacent to the Premises ... including but not limited to selling and display areas, office, storage and employee facilities.” Rel. App. at 5. Those

restrictions are incorporated into Article 6 of the Lease by reference and Article 40 by implication and would thus be binding on any successor Tenant. Rel. App. at 12, 29.

The facts of this case are unique and very uncommon. It is important that they not be misstated. Based on the facts as corrected above, Relator makes the following reply to the arguments raised in Respondent's Brief.

REPLY TO RESPONDENT'S ARGUMENT

I. The tax court did not have, and did not need, jurisdiction over Parcel 0005

Relator agrees that the tax court did not have jurisdiction over Parcel 0005 and could therefore not determine whether Parcel 0005 was properly assessed. That has no bearing on the issue of the value of Parcel 0004. This issue is adequately addressed in Relator's Brief at pages 19–22.

Respondent implies that it was a legal requirement that there be a division of Parcel 0005 and a combination of a portion of it with Parcel 0004. Resp. Br. at 8–9. To the contrary, Minnesota Statutes § 272.16 is inapplicable in this case. That section allows a tax parcel to be split when part of a parcel has been conveyed and the seller and purchaser present that conveyance to the county auditor. A conveyance of a part of Parcel 0005 did not occur here; Parcel 0005 was entirely owned by the owner of the mall in 1992 and on the assessment dates at issue. A combination of the Leased Basement Space with Parcel 0004 was not possible because the two properties had different owners in 1992, and they continued to have different owners at the time of the

assessments at issue. The tax court and Respondent both acknowledge that fact. Rel. Add. at p. 23; Resp. Brief at 10–11.

The solution the parties chose in 1992 is found in Article 10, Paragraph E, and the action taken by the assessor as reflected in the field card for Parcel 004: “New Dayton’s & bsmt of old Dayton’s on this desc. (0004).” Rel. Add. at 16, 65-66. But, most importantly, with or without a combination of tax parcels the value of Parcel 0004 includes the benefit it enjoys from the right it has to operate its department store on the Leased Basement Space, for the reasons put forward in Relator’s Brief.

II. The rights to the use of the Leased Basement Space run with the land of the Subject Property, Parcel 0004.

A. The Subject Property’s right to use the Leased Basement Space is assignable without the need to execute additional instruments.

Respondent states “A purchaser of Parcel 0004 acquires no rights over the Leased Basement Space, or any other portion of Parcel 0005, unless there is a separate legal assignment instrument identifying and transferring said rights in the Leased Basement Space.” Resp. Br. at 12. The tax court gave as its sole reason for finding that Respondent’s rights to the Leased Basement Space do not run with the land the fact that the Lease “requires assignment of the lease to transfer rights under it.” Rel. Add. at 52. The facts belie that conclusion. The terms of the Lease and its history support a finding that the right to use the Leased Basement Space runs with Subject Property without the execution of any additional document.

1. The terms of the Lease.

Article 40 of the Lease provides that the covenants and conditions of the Lease “shall inure to the benefit of Tenant and assigns of Tenant.” Rel. App. at 29. Pursuant to Article 21 of the Lease a transfer to a party acquiring the Main Store did not require the approval of the Landlord. Rel. App. at 21. That stands in contrast to the standard language of Article 40 in the draft lease which required the consent of the Landlord for any succession of interest. Ex. K tab 3 at P-000279. Similarly, the standard language for Article 21 did not have the waiver of the requirement of Landlord approval if the assignment went to “a party acquiring the Main store.” Ex. K tab 3 at P-000274 to P-000275. The effect of the terms as adopted in the Lease is to allow automatic succession to the Tenant’s rights to a party acquiring the Main Store *i.e.* the Subject Property.

2. Conduct of the parties.

The rights to the Leased Basement Space granted in the Lease *were* automatically acquired by the successor in interest to that Lease when the ownership of the Main Parcel changed. Dayton’s sold the Subject Property to May in 2004. Rel. Add. at 60. The fact that May succeeded to the rights of the Tenant to the Lease is acknowledge in a letter from the Landlord in 2006 referring to “The May Department Stores Company, successor to Dayton Hudson Corporation, as tenant.” Rel. App. at 37. There is no document of record that was used to transfer or assign the rights under the Lease when that succession occurred

in 2004. None was necessary because the rights attached to the Subject Property and were acquired by the new owner of the Subject Property by virtue of that ownership, as the Lease provided it would be.

Thus, the implementation of the Lease supports Respondent's position that the rights to the Leased Basement Space therein run with the Subject Property. Those rights were fully assignable to the successors in interest to the original Tenant and, in fact, were assumed by May (which subsequently merged to become Respondent) without the execution of an assignment of the Lease.

B. The holding of County of Du Page supports Relator's argument that property values for tax purposes should reflect the benefits provided by an adjoining parcel.

The disposition of the Illinois case cited in Relator's and Respondent's briefs, County of Du Page v. Property Tax Appeal Board, 708 N.E.2d 525 (Ill. App. Ct. 1999) [hereinafter County of Du Page II], is controlled by the Illinois court's earlier analysis in County of Du Page v. Property Tax Appeal Board, 660 N.E.2d 985 (Ill. App. Ct. 1995) [hereinafter County of Du Page I]. County of Du Page II, 708 N.E.2d at 528. And, in the earlier case, the court noted that "[t]he parties have not cited any case addressing this precise issue, and our research has not uncovered any." County of Du Page I, 660 N.E.2d at 988. Respondent describes County of Du Page II as a case involving a "classic 'right of way' easement, in which the dominant parcel was carved out of and surrounded by the servient parcel." Resp. Br. at 13. The court would not have found a dearth of case

law if the issue could have been resolved on basic, well-established easement principles.

Instead, the Illinois court in both cases found that a property's value may be increased because of the right to the use of an adjoining parcel, which right was conveyed through a lease. County of Du Page II, 708 N.E.2d at 528; County of Du Page I, 660 N.E.2d at 989. As the court stated in County of Du Page I, "each set of parcels is worth more by being located near the other." 660 N.E.2d at 989. In other words, the added value is a by-product of the parcels' relationship with each other. Thus, a valuation for tax purposes must include this benefit because "a tax assessment must include all interests in the property." County of Du Page I, 660 N.E.2d at 988 (citing Homer v. Dadeland Shopping Center, Inc., 229 So.2d 834, 837 (Fla. 1969)).

Contrary to Respondent's interpretation of the case, the Illinois court does not confine its holding to situations involving easements. In fact, the parking rights arose from a lease. "Pursuant to the terms of [the Lessee's] lease agreement with the owner of the shopping center, [the Lessee] has the right to use certain common areas of the shopping center." County of Du Page II, 708 N.E.2d at 526. The reference to an easement cited by Respondent is derived from the court's paraphrase of the county's argument. County of Du Page II, 708 N.E.2d at 527 ("The county argues that the Tax Appeal Board erred by subtracting the value attributable to the parking facilities and common area easements from the assessed

value of parcel 027.”) (emphasis added). Language concerning easements does not appear anywhere in the court’s analysis in either case. County of Du Page II, 708 N.E.2d at 527–28; County of Du Page I, 660 N.E.2d at 988–89.

Though not binding authority, the Illinois court’s holdings in County of Du Page I and II are applicable to this case. Like the adjoining parking lots presented in those cases, the Leased Basement Space is on an adjoining parcel, the use of which contributes value to the Subject Property. As in those cases, the tax court should not ignore this additional value merely because the right to enjoy the benefits of using the adjoining parcel is granted in a lease.

C. Leased fee and leasehold estate have no applicability to the valuation of Parcel 0004.

Respondent’s discussion of “leased fee” and “fee simple” is arguing a concept that is not applicable here. As this court has recently noted, a “leased fee interest is limited to the current landlord’s interest in the property”

Continental Retail v. County of Hennepin, 801 N.W.2d 395, 401 (Minn. 2011).

Likewise, the “leasehold estate” would be the current tenant’s interest in the property. Those interests are specific to the current landlord or tenant. In this case the “leased fee interest” and the “leasehold estate” would relate to Parcel 0005, the subject of the Lease. Neither the fee simple, the leased fee nor the leasehold estate of Parcel 0005 is at issue in these proceedings. Here, the court is valuing the fee simple—the entire bundle of rights—of Parcel 0004. Pursuant to Minnesota

Statutes § 272.03, a statute Respondent completely and inexplicably ignores, the bundle of rights must include *all* rights that belong or appertain to the land [Parcel 0004]. Because the right to the use of the Leased Basement Space runs with the land [Parcel 0004] the enhancement of Parcel 0004's value due to Parcel 0004's rights in the Leased Basement Space must be taken into account.

III. Taxation of Parcel 0005 is not at issue.

Respondent's argument that the value of the Leased Basement Space is already being taxed as part of Parcel 0005 is based on the chart it proposes at page 17 of its Brief. That chart is misleading because it gives only gross building areas. The proper unit of comparison is net rentable area, which would be substantially smaller than gross building area for the Main Mall parcel and would indicate a much higher "AEMV PSF" for the Main Mall Parcel. To compare the gross area of the mall, which includes large areas of unleased open space, with store space that is almost entirely leased is misleading. No meaningful conclusions can be drawn from that comparison, nor does there need to be. The tax court correctly observed that it did not need to—and was not making—any finding as to whether the Leased Basement Space was being double taxed. Rel. Add. at 23. Neither does this court need to address that issue.

CONCLUSION

The tax court erred when it stated that the rights to the use of the Leased Basement Space conferred by the Lease did not "run with the land" of the Subject Property. Under

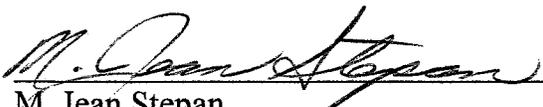
the unique facts presented in this case the right to use the Leased Basement Space as part of the operation of the Subject Property “belongs or appertains to” the Subject Property. It is part of the “real property” being valued as defined by Minn. Stat. § 272.03, subd. 1(a). The fact that the tax court did not have jurisdiction over Parcel 0005 is irrelevant to a determination of the Subject Property’s value.

This Court should find that as a matter of law the right to the use of the Leased Basement Space belongs to and appertains to the Subject Property for the years at issue and that the value to the Subject Property of the use of the Leased Basement Space must be included in the value of the Subject Property for purposes of property taxation. The tax court should be directed to re-determine the Subject Property’s value including the value contributed to the Subject Property by its right to the use of the Leased Basement Space as part of its department store.

Respectfully submitted,

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Dated: January 26, 2012


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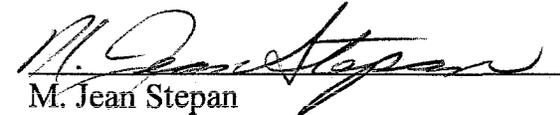
Respondent.

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01, subs. 1 and 3, for a brief produced with a proportional font. The length of this brief is 3,376 words. This brief was prepared using Microsoft Word 2007.

Dated:

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